DOCUMENT RESUME

ED 045 055 HE 001 900

TITLE	Harvard and Money: A Memorandum on Issues and Choices.
INSTITUTION	Harvard Univ., Cambridge , Mass. Univ. Committee on Governance.
PUB DATE	Nov 70
NOTE	37p.
EDRS PRICE	EDRS Price MF-$0.25 HC-$1.95
DESCRIPTORS	*Educational Finance, *Financial Needs, *Financial Policy, Financial Problems, *Higher Education, Investment, *Money Management, Resource Allocations, Tuition
IDENTIFIERS	*Harvard University

ABSTRACT

This report discusses some of the financial issues and choices with which Harvard University will have to cope in an environment of increased stringency: issues of money-allocation, money raising, and money management. Part I presents highlights of Harvard's recent financial history and its prospects in quantitative terms. Part II presents some general guidelines for the discussion. Part III discusses money spending and raises such issues as: (1) should "every tub on its own bottom" (ETOB) remain the principal rule of allocation; (2) if the scope for central decisions widens, what machinery is likely to produce good choices; and (3) should part of the University's money be spent on non-Harvard charities? Part IV deals with money raising and such questions as: (1) what strategy will raise the most gift money from private sources; (2) is it possible to loosen the link between the way money is raised and how it is spent; (3) government money; (4) the level of student tuition; and (5) improved exploitation of Harvard's physical plant. The final section deals with money spending and such questions as if only money mattered, what criteria and what machinery would be appropriate for guiding investment of Harvard's portfolio; and if not only money matters, what non-financial guidelines should Harvard observe. (AF)

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THE UNIVERSITY COMMITTEE ON GOVERNANCE
HARVARD UNIVERSITY

EDO 045055

Harvard and Money
A Memorandum on Issues and Choices

CAMBRIDGE, MASSACHUSETTS
NOVEMBER 1970

HARVARD AND MONEY

A Memorandum on Issues and Choices

- Does Harvard have a responsibility for the social conduct of the hundred-odd corporations in which the University owns stock?
- Should any part of Harvard's $1 billion portfolio be invested in socially beneficial activities that do not offer a financially attractive combination of yield, growth, and risk?
- Who is to decide? Through what procedures? By what criteria?

These have been the headline issues involving Harvard and money. Obviously, they constitute only a small, special class of the many financial questions facing the University. Most of the other questions are less dramatic, but some are equally urgent and may be even more difficult and subtle. For instance:

- Is Harvard threatened during the next few years by a financial "crisis" of a magnitude already confronting universities like Columbia and even Yale? If so, what strategy should guide the University's response? Are more or less proportional cutbacks preferable to the outright elimination of one or more major activities, even Schools?
- In any event, how should Harvard allocate its resources between renaissance history and high energy physics? marketing and Sanskrit? law, education, design, and arts and sciences? undergraduate scholarships, post-doctoral fellowships, faculty salaries and Widener Library?
- What are the prospects for the flow of gifts to the University, and of suitable private and public contract money? Can Harvard's machinery for raising new money be strengthened? What kind of restrictions on gifts and on contract money are and are not acceptable?
- How much of the money available to the University should be spent today, and how much accumulated for the future?

As a matter of prudent economics, do capital gains in the portfolio differ in kind from dividends and interest? As a matter of law, how much freedom does Harvard have to spend realized capital gains?

- What is the appropriate pattern of tuition and scholarship and subsidized loans? Should Harvard continue to hold tuition below cost, thus in effect "subsidizing" students from prosperous families and students whose education is likely to make them prosperous in the future? What is the measure of cost? What defines prosperous?

- And, once again, *who is to decide, by what criteria, through what machinery and procedures?*

The questions pertaining to social investment by Harvard (itself a charity), and its responsibilities as a stockholder, are "new"; they reflect recent currents of social sensibility and politics. The rest, and others like them – many of which bear on the central functions of the University – are old, but may have to be answered anew, following different procedures and applying new standards, in a time of trouble when money is likely to be scarcer relative to widely perceived needs than during the past two decades.

The mandate of the Committee on Governance is to recommend changes in governing structures and procedures, not to offer solutions to "substantive" problems. Moreover, a university is not a business; most of the most important choices have to be measured in a metric not defined in dollars. Still, one way or another almost all important choices do involve money, and at the edges, where it counts, are constrained by money. And structures and procedures cannot be judged in the abstract; judgment must reflect the problems that governing institutions are supposed to solve. "Solutions," in turn, that do not specify the machinery of choice and implementation rarely solve any problem. More often, they beg it.

The purpose of this preliminary memorandum on Harvard's finances is to discuss some of the financial issues and choices with which Harvard will have to cope in an environment of increased stringency: issues of money-allocation, money-raising and money-management. Some will be on the front burner of university politics. Almost all raise fundamental questions of purpose and

value bearing on the nature, role, and significance in the United States of large private universities committed to the ideal of intellectual eminence. All the estates of the University: faculty, students, governing boards, and alumni, have a legitimate stake in the answers. And they all have both voice and power. So does the larger community outside, whether in the immediate neighborhood or in the country at large as represented in Washington.

It is in the nature of questions involving values that reasonable men can and usually do differ. The writers of this memorandum cannot claim to be neutral. But we have tried not to load the questions. Our intent has been to pose issues in terms that will fairly represent the convictions and puzzles in the minds of the members of the various constituencies – puzzles about their own thought, more often about that of others.

Our objective is to identify and define differences, narrowing these where we can, sharpening them where clarity demands. Nevertheless, some will find the very questions we have posed out of order, even obnoxious. Those who believe that Harvard as a corporate citizen of Boston and Cambridge has no responsibilities that go beyond the processes of learning, will find the paper unsatisfactory not merely in execution but in its premises. So will anyone who believes that Harvard's primary concern is other than learning, broadly defined. Certainly, the paper will fail to satisfy those few who believe that the best thing Harvard could do with its endowment would be to give it away to poor people, and the next best, to dump it in the Charles on the ground that Harvard is a servant of evil in an evil society and the sooner it goes out of business, the better.

Putting it positively, the discussion takes as given three value judgments:

1. The preeminent task of Harvard remains the advancement of learning; further, our paramount and continuing problem is to improve our performance in the pursuit of learning.*

2. Private universities that strive for intellectual eminence, and hence are on one definition "elitist," have a valuable role to play in America.

* As Mr. Whitehead once put it: "uniting the young and the old in the imaginative consideration of learning." (Quoted in McG. Bundy, "Were Those the Days?" *Daedalus*, Summer, 1970.)

3. The University's obligations as a corporate citizen are not fully discharged by working toward excellence in its primary mission. Harvard has a corporate responsibility to take into account other facets of its economic and social impact on its neighborhood and community.

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The body of the memorandum is organized under five headings: I. Recent Quantitative History and Prospects: Highlights; II. Guidelines for Discourse; III. Money Spending; IV. Money Raising; V. Money Management.

I. Recent Quantitative History and Prospects: Highlights

1. Table I underscores a number of facts about Harvard's "operating" income and expenses. Specifically:

— Between 1949 and 1969, the University's operating budget has grown six-fold; in the last ten years, by a factor of about two-and-a-half. (The general price level in the U.S. between '49 and '69 increased by 62%. Excluding the summer school and extension courses, Harvard's enrollment grew from 11,308 in '49 to 15,349 in '69, with all of the increase occurring during the '60s, and virtually all in the graduate and professional schools. During the same twenty years the number of "officers of instruction and administration" almost tripled, rising from 2,712 in '49, to 4,206 in '59, to 7,953 in '69.)

— As striking as the growth in the total operating budget is the change in the sources of operating income. The proportion provided by government contracts and grants increased from 8% in '49, to 19.4% in '59 and 36.2% in '69. The share contributed by tuition and fees (including charges for board and lodging) declined from 42.8% in '49, to 31% in '59 and 21.4% in '69. (The relative contribution of tuition net of scholarships declined even faster; the share of scholarships in total operating expenses grew from 4.6% to 6.4% to 9.7%.)

— Together, government money and expendable gifts accounted for less than a fifth of operating income in 1949, somewhat more than a third in 1959, and slightly more than half in 1969. The University as it is today depends for half of its

TABLE I
OPERATING INCOME AND EXPENSES

Income	1949	1959	1969	1949 %	1959 %	1969 %
Capital fund income availed of	7.0	16.0	36.2	24.2 %	23.7 %	20.6 %
Gifts for current use and other receipts for special purposes availed of	3.3 [1]	11.6	26.5	11.2 %	17.3 %	15.0 %
Tuition and other fees	12.4 [2]	15.0	29.8	42.8 %	22.3 %	16.9 %
Board and lodging		5.8	8.0		8.7 %	4.5 %
Reimbursements of government grants and contracts	2.6 [1]	13.0	63.7	8.0 %	19.4 %	36.2 %
Receipts from other sources, including athletic gate receipts and sales of publications, printing and power	3.7	5.8	12.0	13.8 %	8.6 %	6.8 %
TOTAL INCOME	29.0	67.2	176.2		100.	
Expenses						
Salaries of Corporation appointees	7.7	17.6	43.2	27.2 %	26.7 %	24.6 %
Wages	9.1	18.2	41.9	32.1 %	27.8 %	23.9 %
Equipment and supplies	6.4	12.6	28.9	22.5 %	19.1 %	16.5 %
Retiring allowances and other employee benefits	.9	3.3	11.6	3.0 %	5.0 %	6.6 %
Scholarships and other student awards	1.3	4.2	17.0	4.6 %	6.4 %	9.7 %
Other expense including travel, telephone and sundry services purchased, certain expenditures for non-departmental projects	3.0	9.9	32.9	10.6 %	15.0 %	18.7 %
TOTAL EXPENSES	28.4	65.8	175.5		100.	
Transfers to departmental balances	.5 [3]	1.4	.7			
TOTAL EXPENSES AND TRANSFERS	29.0	67.2	176.2			

(For fiscal years ended 30 June; figures stated in millions of dollars.)

1. The figure differs from that reported in The Treasurer's *Financial Report* because in 1948–49 the *Report* classified U.S. Public Health receipts as "gifts for current use."
2. Tuition and other student income including board and lodging.
3. Discrepancy from *Financial Report* due to rounding.

operating income on constituents residing outside of Cambridge.*

2. The different Schools are not equally dependent on moneys which lie outside of the University's control. Table II gives a vivid picture of the differences among Schools according to their relative dependence on sources of differing dependability. Those differences are a critical feature of Harvard. Since the early 19th century, and certainly since the presidency of Mr. Conant, the University has operated on the principle that, over time, each "unit" should by and large finance itself. "Every tub on its own bottom" (ETOB), though not enforced with uniform stringency, has dominated the allocation of financial resources. The governing strategy for raising new money, it has powerfully affected the University's shape.

3. ETOB, in combination with the host of specific restrictions on specific gifts agreed between the donor and the member of the University pursuing him, has had two related, specific consequences worth noting.

— Only a small fraction of the total resources on Harvard's books are freely available for allocation by the President and Fellows, or even for significant reallocation except within narrow limits. Most of Harvard's money is not fungible. Although there is a good deal more flexibility within Schools than among them, there are significant constraints on reallocation even within the Schools, especially in Arts & Sciences. Financially, Harvard is a confederation of semi-independent baronies, squirearchies, and small farms.**

— The fortunes of each School and "tub" have been exceed-

* Tables I and II do not shown capital expenditure either on construction or on new professorships, increases in scholarship endowment and the like. (The Financial Report of the Treasurer does not contain a summary table which breaks down total capital expenditures by "object".) In 1968–69, Harvard spent $16,806,000 on plant; during the past ten years, average annual construction spending amounted to $13,512,328. In 1968–69, the University received gifts for capital totaling $29,460,144. The ten year annual average of such gifts was $28,115,277. (None of the ten year figures is adjusted for inflation: we have added '69 dollars to '68 dollars to '67 dollars, etc.)

For additional information on gifts for capital, see Table III, p. 12.

** As a purely *legal* matter, the Corporation could of course lay claim to the $30,000,000 of tuition receipts, and redistribute the money as it sees fit. Indeed, it could charge the richer Schools rent at commercial rates. But as a political matter, subject only to the possibilities discussed on pp. 27–28, that is not in the cards.

TABLE II

SOURCES OF OPERATING INCOME [1]

1968–69	Capital fund availed of	Gifts for current use	Tuition and other student income	Reimbursements of government grants and contracts	Other receipts	Total income
Arts & Sciences	22.3 %	13.7 %	23.9 %	34.3 %	5.8 %	$68,096,346
Business Administration	8.7 %	40.7 %	41.6 %	3.3 %	5.7 %	15,075,168
Dental	20.7 %	7.3 %	9.7 %	58.6 %	3.6 %	1,790,235
Design	39.8 %	11.0 %	28.3 %	20.2 %	.8 %	1,886,520
Divinity	61.3 %	16.0 %	17.3 %	.5 %	5.0 %	1,386,057
Education	11.5 %	29.5 %	15.2 %	42.8 %	1.0 %	7,720,505
Kennedy School	49.1 %	11.4 %	12.7 %	16.7 %	10.0 %	1,560,213
Law	20.2 %	18.2 %	53.5 %	5.6 %	2.6 %	6,587,249
Medical	13.1 %	10.2 %	7.2 %	65.7 %	3.9 %	28,334,105
Public Health	11.5 %	12.8 %	3.2 %	71.1 %	1.3 %	7,738,248
University, Non-School	50.2 %	.3 %	.6 %	—	48.9 %	7,946,874
University-wide Total	20.6 %	15.0 %	21.4 %	36.2 %	6.8 %	$176,293,258
Radcliffe	16.3 %	13.8 %	68.2 %	.0 %	1.7 %	$7,013,817

1. Percentage may not add up to exactly 100% due to rounding.

ingly sensitive to the pocket-books and loyalties of its own alumni; the popularity of its subject matter among rich patrons, foundations, and the government; the income-status and expectations of its students; and in some cases, to the general state of the Federal budget. It is a fair presumption that fiscal austerity in Washington will hit the School of Education harder than the Law School.

4. Despite ETOB, the center has not been entirely impotent. There is more power available to the President and Fellows than meets the eye.

— Some "old" money is unrestricted and hence available for allocation by the center. Restrictions on some other old money leave quite a lot of room for maneuver. (Measured by degree of flexibility, it is apparently possible to identify fifteen different categories of restriction.) Judicially used at the margin, free and relatively free money can make a great deal of difference. The President and Fellows have taken advantage of the availability of unrestricted income (dividends and interest) to channel funds to priority activities.

— In the course of helping to raise new money, the President has a lot of leeway in advising donors about needs and priorities, and influencing access to particular donors by individual Schools and Departments. Depending on how much use the President, or within Arts & Sciences the Dean, wishes to make of this influence, each can have a good deal to say about where the new money goes. (According to an informed estimate, in allocating newly endowed professorships in Arts & Sciences among fields and departments during the last decade, the Dean has had a wide range of choice in about a quarter of the cases and significant influence in another quarter.)

Nevertheless, the amount of discretion available to the center in the allocation of money has been exceedingly limited. It is fair to say that the present shape of Harvard reflects some 300 years' worth of bargains between generations of presidents, deans, professors, and administrators, on the one hand, and donors on the other.

5. Until this past July, and especially since World War II, Harvard's bookkeeping system produced a strong bias in favor of relatively newly financed activities as against the old. The

individual restricted accounts were carried at *book* value and participated in earnings from the General Investment Account (where most of the money is invested on a co-mingled basis) in proportion to book value. To be sure, the Corporation periodically authorized distribution of capital gains realized in the Investment Account to the various earmarked accounts, and such distributions increased the book value of each such account. But participation in those periodic distributions has also been kept in proportion to book value, and hence $1 received by an account just before a distribution would participate equally with $1 which had been distributed to an account four years previously, and equally also with $1 originally given 200 years ago. Obviously, the book value rule has favored relatively new activities over old.

In the face of a threat of legal action, the University on July 1 of this year shifted from book value to a unit system of accounting. Under a unit system, capital gains and losses are automatically reflected by the separate accounts, and hence each account will participate in the income earned by the portfolio as a whole (as well as in capital gains) in proportion to its continuously updated *market* value. (Insofar as the terms of the deeds permit, the budget process will leave final power over the *spending* of its own capital gains by each "tub" in the hands of the Corporation.)

6. Evidently, under the unit system, restrictions on new money, as on old, will give rise to a much more "conservative" lockstep than in the past. The University's policy on restrictions therefore has become a matter of great importance. In recent history, Harvard appears to have imposed only three general rules:

— No donor has been given the right to forbid any activity financed by other than his own money, or to impose "political" restrictions such as would constrain the freedom of ideas. Some offers of gifts have been turned down because they would have violated this rule.

— The University has not undertaken work that had to be "classified." (Individual professors have been free to engage in classified consulting on their own when they so chose.)

— With very few exceptions, involving very exceptional cases, the University has required that the salary cost of tenure appointments be fully financed by money under Harvard's con-

trol (endowment income supplemented by tuition the University could safely count on).

7. Two secondary effects of the decentralized mode of allocation implied by ETOB warrant special comment:

— There does not exist at the center a store of systematic knowledge about the shape of average and marginal costs of various University activities which would throw light on potential cost trade-offs among them. Some Schools, notably Business, have set up central cost-accounting procedures. But Harvard does not possess, on a university-wide basis, a reporting-accounting procedure that generates the information that would be needed for systematic "planning-programming-budgeting."

— A number of important joint activities that benefit all the Schools: Widener Library, computer facilities, etc., have been exposed to the hazards of all things that are both everybody's business and nobody's. If many such overhead activities have nevertheless fared well, the credit is due both to the prosperity of the times and the extraordinary exertions of a dedicated few.

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What about the future? The outlook for the next few years is bleak. The long term prospect, though less certain, is also bleak. The entire private university system in the United States, in its current form, is in grave financial trouble. Although richer than the others, Harvard is no exception.

The reasons for the trouble are plain:

1. Without drastic changes in the way universities go about their teaching business, average cost per student, excluding organized research, is likely to rise at rates two to three times greater than the general price level for the entire GNP. William Bowen's study of eight universities, including Harvard, Princeton and Yale, found that "educational and general expenditures per student (excluding organized research) increased at an average annual rate of 8.5% between 1963–64, and 1967–68." During the same period the price index for the GNP rose at an average rate of about 2.5%. The causes have been many: new areas of instruction have grown up; resources going into teaching, and into research closely connected with teaching, have become more ex-

pensive; the proportion of graduate students in the student body has increased, and they are more expensive than undergraduates. In general, and however measured, "productivity" in education, as in services generally, has not kept pace with productivity in other sectors of the economy.

Some of the above tendencies will persist, others not. Barring radical reform in teaching methods, Bowen's projection of a 7.5% annual increase in cost per student is unlikely to be too high. This would mean that, with no change in scale or scope, merely standing still would require Harvard to double its operating budget by 1980. (To be sure, stringency of money will itself tend to slow the process of inflation; the cost of professors and of talented students to universities reflects both supply and demand. On the other hand, the large private universities may face increasingly severe competition for both faculty and students from their public sister institutions.)

2. Assuming that costs will continue to increase at a rate significantly faster than inflation in the economy as a whole, what about prospects for the supply of money? One has to distinguish among sources.

— If one ignores short term fluctuations and concentrates on the long term, Harvard's large portfolio may be the one bright spot in the picture. Since no numerical measure of past performance is publicly available, it would be foolish to assert that we ought to be able to do better in the future. But it is possible that a more flexible exploitation of endowment money, with due regard for the protection of the corpus against erosion by inflation, would give Harvard an even greater financial advantage over other private universities than it has enjoyed in the past.

— Private gifts raise a serious question mark. In the past, alumni as well as others have been most generous to this University. But will they remain so? Probably, but a lot may depend on how well we cope with our internal difficulties. During the past two years, alumni gifts have declined significantly. Uncertainty about the new tax law and malaise in the stock market may have had much to do with it. Nevertheless, everyone concerned with the welfare of Harvard must keep the problem in mind. (Table III contains a summary of gifts in various categories since 1965–66.)

TABLE III

SUMMARY OF GIFTS 1965–1970

	Trusts and Bequests							
1965–66	Alumni	Non-Alumni	Alumni	Non-Alumni	Corporations	Foundations	Others	Totals
Capital	$ 6,496,476	$10,474,607	$ 3,966,941	$ 1,993,306	$ 2,357,127	$ 3,996,909	$ 78,646	$29,364,012
Current Use	113,095	460,934	4,210,011	1,030,400	2,571,001	6,218,739	496,063	15,100,243
Total	$ 6,609,571	$10,935,541	$ 8,176,952	$ 3,023,706	$ 4,928,128	$10,215,648	$ 574,709	$44,464,255
1966–67								
Capital	$ 4,350,051	$ 1,982,632	$ 3,914,976	$ 1,610,113	$ 2,463,195	$ 4,492,448	$1,219,699	$20,033,114
Current Use	108,652	467,986	5,113,448	526,338	4,175,175	7,446,225	475,173	18,312,997
Total	$ 4,458,703	$ 2,450,618	$ 9,028,424	$ 2,136,451	$ 6,638,370	$11,938,673	$1,694,872	$38,346,111
1967–68								
Capital	$16,351,402	$ 3,019,430	$14,847,126	$ 1,407,217	$ 2,162,725	$ 7,298,813	$ 400,777	$45,487,490
Current Use	92,546	557,824	5,549,969	1,516,046	4,374,108	7,689,190	758,543	20,538,226
Total	$16,443,948	$ 3,577,254	$20,397,095	$ 2,923,263	$ 6,536,833	$14,988,003	$1,159,320	$66,025,716
1968–69								
Capital	$ 2,001,217	$ 1,524,004	$ 9,556,021	$ 5,316,653	$ 2,637,177	$ 8,194,282	$ 230,790	$29,460,144
Current Use	307,192	62,444	6,504,568	982,558	4,004,761	8,737,534	888,567	21,487,624
Total	$ 2,308,409	$ 1,586,448	$16,060,589	$ 6,299,211	$ 6,641,938	$16,931,816	$1,119,357	$50,947,768
1969–70								
Capital	$ 4,143,681	$10,628,797	$ 4,506,563	$ 2,888,776	$ 1,516,130	$ 4,786,502	$ 116,007	$28,586,456
Current Use	1,162,589	1,048,605	5,710,278	1,106,623	5,062,626	8,478,797	941,032	23,510,550
Total	$ 5,306,270	$11,677,402	$10,216,841	$ 3,995,399	$ 6,578,756	$13,265,299	$1,057,039	$52,097,006

Gifts to Harvard totalled $657 million in last twenty years.

– Sale of "services," especially the tuition/scholarship/loan-fund mix, provides an important area of flexibility, subject to the constraint of competition for first rate students not only from other private but also from public universities. (In this area, there exists a powerful case for a new and uniform national policy.)

– What about government as a source of money? During the past twenty-five years, a discrepancy has arisen between the stated rationale for the rising flow of Federal money to the large universities, and what the universities have in fact been doing.* Such a discrepancy is not likely to persist. For the near future, the key question is whether a politically compelling rationale can be found which would not at the same time require the large universities drastically to change their character. For the longer term, one must face the deeper question: are there major changes in what we do and how we do it that would enable us better to exploit Harvard's true comparative advantage in the pursuit of the higher learning, and also provide a basis for whatever public support we may then need?

To conclude: The proposition that Harvard is rich is at best misleading. In the absence of major change in the way the University goes about its business, and perhaps even then, the new president is likely to face severe financial difficulties. Relative to widely felt needs, money has been scarce all along. It is likely to become a good deal scarcer. In the next decade, Harvard's governing institutions will face hard decisions about what activities are to stand still, or shrink, or even disappear. That will certainly be the case if the University is to undertake new ventures which are not popular enough to finance themselves.

Over the long run *both* structural change and new kinds of finance may be necessary if Harvard is not to deteriorate in scope, range and intellectual quality. An important task of the new president may well be to take the lead among private and public universities in developing a politically viable plan for reorganizing and financing higher education in the United States. Without such a plan, the long term future will remain bleak, though it is probable that of the large private universities Harvard would be the last to go down.

* See Carl Kaysen, *The Higher Learning, the Universities, and the Public,* Princeton University Press, 1969.

The rest of this memorandum does not address these large issues. Any serious discussion of those must begin not with questions of money, but with the prior question of what the American university system ought to be about during the next two–three decades, and where an institution with Harvard's special history and assets might best fit. Our purpose here is to raise for discussion the financial issues that face the Harvard of today.

II. Guidelines For Discourse

Questions involving the University and money are both complicated and controversial. In the course of our discussions on the subject, some general propositions have suggested themselves which, if acceptable, make it easier to identify the boundaries of agreement. We commend them to the community at large. In any event, since they color the treatment of substantive questions in what follows, we wish to make them explicit.

1. Because money will be scarce relative to widely felt needs, the benefits of spending more on something must be weighed against the costs of spending less on something else of significant direct value to members of the University. To propose more money for scholarships and less for buying stock in the portfolio (which, in itself, is not a "final" value) is to beg the problem. Needless to say, an argument in favor of more money for scholarships today and less for something of "final" value tomorrow is perfectly legitimate.

2. There does not exist a coherent model of the university that would compel agreement on priorities and choices. The principle that choices should follow agreement on "goals" is, at the level of unconstrained logic, unassailable. Moreover, continuing debate about the goals of universities in general, and Harvard in particular, is valuable in itself. But we suspect that any consensus on goals will leave a great many of the large financial issues facing the University unresolved, and not merely those which have to do with the raising of money. It is well to recognize that no agreement exists or is possible which is sharp enough to yield answers to difficult financial choices.

   Even the "classical" model of the university: a place

where learning is pursued according to the lights of individual professors and organized around coherent disciplines and professions, leaves open a host of difficult choices. Which fields are to be nourished by new money, and which allowed to languish? What new fields or combinations should be created? How should money be divided between professorial salaries which affect Harvard's ability to attract and hold scholars of eminence, and scholarship aid which in turn affects Harvard's ability to attract students from poor and lower-middle income families? Agreement that "learning" is *the* mission of the University does not imply answers. (The problem is complicated by the fact that there are some members of the University who would, in any case, put more emphasis on direct service to the community.)

3. On its face, there is something peculiar about the notion that it is somehow right for a great university to be shaped more or less by happenstance, by the largely uncoordinated entrepreneurial activities of deans, professors and administrators, and the proclivities of donors. No doubt, "every tub on its own bottom" has much to commend it. It sidesteps a good many unresolvable arguments about purposes; decisions about the shape of the University are ad hoc, sequential, and by and large implicit. But so are the results. (The proposition that such a regime is "right" *because* every activity which survives is "self-supporting," is indefensible. This is not a domain where one can count on Adam Smith's invisible hand to make "competition" efficient in serving any reasonable set of values.)

4. As in all spheres where reasonable men can disagree about ends, legitimacy of decision in the University is largely a function of procedure. If we are to move away from "every tub on its own bottom" toward more explicit choice – or, to take another controversial question, make explicit value judgments about the social conduct of particular companies in which Harvard owns stock – we shall have to devise machinery that will command widespread support from all the constituencies. For they all have interests at stake – and competence and power – though in varying degree and kind, depending on the question. Moreover, the underlying raw power is not generally distributed in proportion either

to the legitimacy of the interest or to the depth of the competence. It is the more important that in promoting particular kinds of machinery to deal with particular classes of questions, each constituency should keep in mind all the others.

5. The mood of the moment is for "open decisions, openly arrived at." Yet it is not obvious that "democratic" processes, even if weighted by considerations of competence, will produce a significantly better University for the future than, say, a strong, accountable president with vision and a creative talent for generating consensus. Moreover, it is well to remember that non-hierarchic, explicit, participatory processes impose large costs. They disperse responsibility. They are vulnerable to empire protection, logrolling, and the like. And they exact a high price measured in divisiveness, and in the time and energy of people whose competence may not reach the particular question at hand and whose special skills do not include the political art of constructive accommodation.

   It is not, of course, a matter of either/or. Indeed, in a situation of budgetary stringency it is difficult to deny the case for somewhat more explicit procedures of decision about money-spending than Harvard has suffered in the past, and somewhat wider participation in such decisions. The problem is to find procedures that will both command support and justify it.

6. In principle, institutions are responsible for the consequences of actions "they" take. But who or what is "they"? The meaning of collective morality – particularly the morality of an institution some of whose members' business it is to "do their own thing" – poses slippery moral questions. The problem becomes especially intractable when institutions that are not hierarchic in organization or coherent in membership make *explicit* "moral" judgments, as institutions, outside their areas of central competence.

   The above argues for a distinction between actions that impinge in direct, perceptible ways on identifiable individuals or groups, and actions whose effects are mainly "symbolic." Obviously, there exists no sharp divide. The domain is likely to be continuous and a boundary very hard to draw.

But in a crude way the distinction is nevertheless useful and important. There is a difference of kind between the consequences of Harvard's actions, indeed its very existence, for the housing market in Cambridge, and the effects of its vote as a stockholder on the behavior of General Motors. There is also a difference between a G.M.-like situation, and situations where the size of Harvard's investment in a company gives it an influential voice in corporate decisions. This is not an argument for ignoring "symbolic" effects. It is an argument for recognizing them for what they are.

7. Last: money-spending, money-raising, and money-management are not separable subjects. Answers to questions under one heading are likely to have consequences for options under the other two. It follows that any prescription for spending must take into account effects on money-raising and money-management, and so on. For example:

   — Even if "every tub on its own bottom" should turn out to be the best strategy for maximizing the amount of new money given to Harvard, if it imposes a pattern of spending that violates widely held and well reasoned views about the shape of the University, one might wish to consider alternative strategies that produce fewer dollars in total, but more free dollars or dollars for higher priority purposes. One might also consider taxing the income or even the principal of restricted money. The value of a dollar is not necessarily a dollar.

   — Seemingly capricious labeling by Harvard of some corporation as a bad citizen (and, by implication, according other corporations at least relative virtue), by a standing vote of a Harvard faculty following a few minutes discussion, might have consequences for Harvard's ability to raise money, at least in the form of donations of shares of the offending company.

   — In an environment of fiscal stringency, if choices between spending today and saving for the future are constrained by the convention that dividends and interest constitute spendable money and realizable capital gains do not, the investment manager may be forced to alter the composition of the portfolio in ways that would reduce total

return without a compensating reduction in risk. (Obviously, where the "convention" reflects the legally binding terms of a deed, the University has little choice.)

* * * *

The raising, spending, and management of money pose for the University a large number of specific issues. Full treatment of any one would require a document as long as the present memorandum. Here, we shall only sketch a few of the central questions in the hope that they will commend themselves to the community for thought and discussion. Such discussion will help the Committee on Governance and other groups and individuals working on these problems as they attempt to formulate concrete recommendations for action. As noted above, we limit ourselves to financial questions facing Harvard as it is today.*

The discussion is organized as follows:

Money Spending

1. Should ETOB remain the principal rule of allocation?
2. If the scope for central decision widens, what machinery is likely to produce good choices?
3. If the scope for central decision widens, what kind of "information system" will make informed choices possible?
4. Should part of the University's money be spent on "non-Harvard charities" – non-competitive social investments that do not contribute directly to the process of learning at Harvard?

Money Raising

1. What strategy will raise the most gift money for Harvard from private sources?
2. Is it possible to loosen the link between the way money is raised and how it is spent?
3. What about money from the government?
4. What "price" should students be charged for a Harvard education?
5. Can Harvard better exploit its physical plant?

* We do not discuss one of the major specific issues facing the University: the financial aspects of merger with Radcliffe. That problem is being given intense study elsewhere.

Money Management

1. If only money mattered, what criteria would be appropriate for guiding the investment of Harvard's portfolio? And what machinery?
2. If not only money matters, what non-financial guidelines should Harvard observe? What machinery would be appropriate for selecting those guidelines and supervising their application?

III. Money Spending

1. Should ETOB remain the principal rule of allocation?

What can be said for it is that it works and that it would be very hard to change. Choices between incommensurable enterprises (accounting and ethics) remain implicit and hence are resolved with a minimum of conflict and pain to the community. It stimulates large numbers of individuals to raise money by requiring those who care about an activity to find money for it. It makes the University relatively sensitive to widely shared perceptions of changing social needs. (The last, of course, may be a mixed blessing.)

Nevertheless, one can make a powerful case for a more centralized process of decision. In a time of financial famine, a system that forces each School to finance itself will save the University neither pain nor conflict; no School or department that is going broke will remain quiet for long. The squeeze on shared facilities, which are not high on anyone's list of needs but necessary for all, may become unmanageable. With new activities unable to raise much new money, the dead hand of the past will increasingly dominate, especially under the unit accounting system which eliminates the advantage of relatively new money over old. In a time when learning may require rapid innovation both in teaching and in research, any system biased in favor of the status quo guarantees obsolescence.

In sum, during the 1970's, survival of the "fittest," where fitness is measured by old money in hand, or by current popularity with the rich or in Washington, is not likely to prove acceptable. Change can come only slowly – most of the money in hand is tied up, and a lot of the new money will undoubtedly be tied up as well. Moreover, rapid change would raise havoc with a host

of special arrangements – more or less tacit bargains among departments and Schools concerning teaching, space and money – in ways that would be difficult to control. Nevertheless, the scope for explicit, centralized choice can be enlarged.

But how would such choice be exercised, and to what end? How is legitimacy to be conferred on decisions about which reasonable men, who have stakes in the matter, will disagree? Continuing debate about goals will be a necessary ingredient. But as suggested above, it will not suffice to yield clear-cut answers in a community that places a high value on freedom of thought and diversity of opinion. Evidently, the crux of the matter lies in machinery.*

2. If the scope for central decision widens, what machinery is likely to produce good choices?

The problem has many dimensions. The key questions are: who should participate, through what procedures, with what kind of power, in what decisions? In the present climate, a president or provost or dean must command the loyalty of his faculty, the support of his financial patrons, and the tolerance of his students. Thus, while working toward coherent objectives, he must anticipate, consult, and persuade, always taking into account his constituents' strongly held views. A strong, perceptive, open minded individual with a farsighted view of his university or school – if he is backed by a skillful staff and, in the case of a president, by deans who command the respect of their faculties and have the welfare of the university at heart – can move a complicated institution toward evolving, not sharply drawn but nevertheless coherent goals. He can search out opportunities, stimulate the imagination and the energies of innovative members of the faculty, build support for good ideas issue by issue, and facilitate constructive compromise. Such an informal process often enables a group of diverse individuals to achieve results that most of them prefer to results produced by more formal machinery. And since the issues and choices run through the mind of a single man, he can be held accountable.

* The question of choice between spending on academic things as against subsidizing social investment is discussed separately in Section 4 (below). Sections 1 and 2 deal exclusively with money choices in the domain of learning. The question of choice between spending today and accumulating for tomorrow is discussed below under Money Management (V).

An important variant of this model – the "collective leadership" version – would place the deans at the center, governing as a cabinet. On any university-wide or major inter-school question, the president or a provost would be "more equal" than his colleagues, but more often than not he would have to command their support. Narrowly intra-school questions would be left for each dean to settle with his own faculty. The style of governance would resemble that sketched above.

At the other end of the spectrum lies full participatory democracy operating through structured, formalized procedures. But as a model for university governance that is surely a straw man; few would favor giving all members, students and alumni as well as faculty, a vote on major budgetary choices. Far less extreme arrangements would violate the canons of considered choice: that those who choose should be competent, have time to consider their choices, and be accountable.

The number and variety of arrangements that would satisfy those canons is large. Each would assign somewhat different roles and powers to administrators, faculty, students, and alumni. And each would offer different prospects for the civility of university life; for the representation of common interests; and for the costs inflicted by the very process of decision, as measured by the drain on faculty and student energies. (It is well to remember the nastiness of academics when dividing money.) More important, each would offer different prospects for the "political" acceptability of decisions, for their financial feasibility, and for their ultimate quality.

We do not propose to sketch the array of possible institutional arrangements. If Harvard should decide to move towards more centralized allocation, it should carefully study the experience of large private universities that do allocate money centrally. Such study should go beyond mere description of institutional forms and attempt to infer, in each case, the organizing principles that govern the participation of the various constituencies in particular kinds of allocation decisions. How are boundaries drawn among classes of decisions: "academic," "student life," etc.? In the assignment of voice, and of power, what weight is given to competence? to the depth and legitimacy of a particular group's interests (and how are those to be measured)? to the duration of deep and active commitment, not merely to particular issues but to the fundamental goal of the university –

to paraphrase McGeorge Bundy, not just to a barony or a discipline but to the kingdom and to learning? and what weight to raw power? The study should examine how well particular arrangements have done, as measured by the tests suggested in the previous paragraph. Last, it should attempt to draw lessons for Harvard, which, for better or worse, is not quite like any other university.

3. If the scope for central decision widens, what kind of "information system" will make informed choices possible?

Would Harvard need a more comprehensive, University-wide system of cost accounting? Should we introduce a full fledged "planning-programming-budgeting" procedure (rolling multi-year program budgets, and the rest)?

Given the premise of question 3., the case for central planning, and for acquiring comprehensive information on which to base it, is easily made. If the center (the President, or a set of deans, or whoever) is to engage in explicit choice between classics and nuclear engineering, it had best know something about the full incremental cost of a professorship in each. In any event, who can gainsay that it would be useful to know the cost of keeping a building open for an extra day, or the Yard grassy? More important, would we not need to know much more than we can now know about the full incremental costs of any large changes in old programs, or of proposed new programs (whether black studies, or faculty housing, or a new departure in general education)? Under ETOB, schools and departments and centers expand, contract, and shift direction, often without facing the longer term financial consequences even for themselves, never mind for others or for the University as a whole. Yet this is an area where, in economists' language, "externalities" abound.

The only possible argument against centralized cost accounting for noneducational support functions – if well done – is that it would cost money and give deans and professors headaches. The question is: would it pay for itself and how soon? A study commissioned by the Corporation should soon throw light on the answer.

Application of elaborate systems of planning in the domain of academic activity poses more difficult questions. In matters of teaching and research in fields as diverse as fine arts and chem-

istry, or music and law, what may seem "fat" to one man may be the heart of the matter for another. How is one to define, measure, and compare *outputs*? Anyone whose job it is to measure is generally tempted to measure what's measurable, thereby leaving out of account what really matters. On balance, the risks would seem to be outweighed by the need for sophisticated, informed thought about alternatives. The problem is to make sure that measurement serves informed debate about policy in support of learning – that it never becomes the master.

Again, the experience of other universities ahead of Harvard in this respect warrants careful study.

4. Should part of the University's money be spent on non-Harvard charities — non competitive social investments that do not contribute directly to the process of learning at Harvard?*

Some members of the University have advocated that Harvard allocate a portion of its budget to non-Harvard charities either by outright gift or by investing in socially deserving enterprises that are financially not competitive.

The question breaks into two. The first and easier part concerns situations where Harvard imposes direct costs on its neighbors. Even there, some would argue that it is up to the government of Cambridge to set the rules; that Harvard's business is to go about its business. But is not the University too big a part of Cambridge to behave as if it were just another citizen? And if so, is it not a part of the University's business in some measure to police itself?

The Wilson Report on *The University and The City* has explored the question in detail. Harvard is acting on some of that Report's recommendations. Specifically, work is going forward on the problem of low-income housing in Cambridge and Boston.** The Committee on Governance is studying the Report's organizational recommendations which were designed to strengthen

* Some will object that the question misses the point — that they advocate investment in projects that are both financially competitive and confer social benefit, as a bonus as it were. That prescription applies less to money *spending* than to money management and is discussed in Section V. In this section we are concerned with spending University money to subsidize social investment that requires subsidy.

** If one doesn't count the input of high-level entrepreneurial energy, low-income housing is a relatively inexpensive form of social investment for Harvard; Federal money provides most of the subsidy.

Harvard's machinery for dialogue with its troubled neighbors and for making prompt response to fair complaint. (In thinking about social investment in Cambridge, one should keep in mind that a perennial complaint of some of the University's neighbors concerns the amount of Harvard's contribution to the city in lieu of property taxes.)

What about general social investment by Harvard when there is no question of Harvard-caused injury? Can any institution with a $1 billion endowment rightly remain aloof from the desperate problems faced by the poor and oppressed? After all, even General Motors spends some money on charity.

Once again the question is, where will the money come from? Who in the University should give up something that he cares about? Opponents of non-educational charity by the University are quick to point out that the use of most of Harvard's money is legally restricted by the terms on which it was given, and that, even if one could get around the law, violating the plain intent of donors is questionable practice. How many donors, they ask, intended that Harvard should serve as a holding company for other charities? Alter all, the University is itself a charity, a social investment. The nation needs more and better higher education, and education is where the University's comparative advantage lies. Or so they argue.*

In judging this debate, one comes up against two hard political facts:

First, the most vocal proponents of social investment are students, whose major institutional affiliation and only leverage on money other than their own is in the University. For them, the University is the most accessible and vulnerable institution subject to pressure in support of social needs which they (and many of the rest of us) consider of utmost national urgency. And quite properly, they are less involved than the administration, governing boards, and faculty in the year-to-year business of keeping Harvard solvent.

Second, however strongly many students may feel, many alumni, and many professors as well — many of whom in both

* Obviously, they would not rule out the many social projects in which members of the University engage in connection with their teaching, research, or other professional activities. They only question the spending of significant sums of Harvard money on social tasks not connected with the University's central functions.

categories share the students' sense of urgency about our national problems – feel as strongly on the other side. And it is the alumni on whom Harvard depends for new money.

If the University is to spend appreciable amounts of money on social tasks not connected with learning at Harvard, it would appear that the alumni must first be turned around – that, on this question, Harvard simply cannot afford a major row with its financial patrons. If so, it follows that, more than in choosing among academic things, the machinery and procedures of decision are critical.

Perhaps more than any other issue, social investment raises the constitutional question: what role should the alumni play in the governance of the University? The relations among the various constituencies, their respective roles and powers, lie at the heart of the conflicts wracking many modern universities. There exists no comprehensive doctrine that commands widespread agreement. Nevertheless, it is well to keep in mind that not all questions are open. At least in the case of Harvard, those who control the preponderance of *raw* power: the alumni and the government, have generally exercised both generosity and restraint. So far, they have not challenged the basic covenants: that in academic matters, in the end the faculty decides – whatever the temptation, alumni must not impose; second, that as long as the University as such keeps out of the political arena (except where its own vital interests are at stake), the government will tolerate and indeed protect non-violent criticism and the expression of unpopular ideas. Tragic examples to the contrary at some other universities underscore the point. "Power to the people," applied literally, shifts the balance of power, not to students or to faculty, but to the alumni and the government. If anyone thinks otherwise, let him study what has happened to higher education in the State of California. Academic freedom is a fragile thing.*

* In the face of the general challenge to authority, and the serious loss of confidence among and within constituencies, it may be that these large questions of constitutional doctrine would benefit from rigorous debate. Such debate would not have to start from scratch. There is wide agreement, not only on the obvious proposition that no single distribution of power is appropriate for all choices, but on many specifics. Few would question the right of each member of the faculty to undertake whatever personal research he may wish as long as he does the rest of his job (that of course begs a part of the problem), does not violate the law, or impose costs on the University beyond his own time; that students should have a predominant say in determining their own life styles, both

IV. Money Raising

1. What strategy will raise the most gift money for Harvard from private sources?

Will the decentralized mode of raising money – the mode of the past, which has forced each School and even department to go after its own money – raise the most money for Harvard as a whole during the 1970s? Even if so, Harvard might want to modify its strategy, since money so raised might not go to the right places. But it is not obvious that a somewhat more centralized approach would reduce the total amount raised. The arguments run both ways.

Decentralization has worked well for Harvard in the past; we have raised more money than any other private university. And it has great advantages. Forcing deans and professors whose purposes require money to raise it for themselves, automatically engages the efforts of many people who are highly motivated, and also well-informed about the specifics of their brief and the inclinations of their patrons. At the same time, the center retains a fair amount of discretion at the edges. A good many of the people who know most about the University's fund raising, and who care about the University as such, continue to believe that the old system is still the best.

Others, some of them not without experience in matters of money, disagree. They advocate that the University switch to a mixed strategy. Specifically, they propose that, from time to time, Harvard launch a major drive on behalf of the University as a whole, an expanded version of the Program for Harvard College of the 1960s. This would first require the University to undertake a comprehensive survey of its needs during the next decade, and to set clear priorities. Then the President, the deans and other central officers would bring to bear the full influence of Harvard

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individually and collectively, as long as the rights of individual students are fully protected and no large amount of University money is involved. Students talented enough to get into Harvard cannot be denied a wide choice among universities. Once here, in choosing among fields and courses, they can and do vote both by voice and with their feet. Alumni retain the right to give or not to give. No doubt, the really hard questions arise where these and other matters intersect. But continuing constructive conversation, designed to identify the difficult areas and to explore them, might help us reach broad agreement on a "social contract." Obviously, the meaning of "learning," and how it is best pursued, would lie at the center of any such conversation.

in presenting an "opportunity for investment" in the University, and specifically in those projects to which the University itself assigns the highest priority.

The arguments advanced in support of a mixed strategy are several. Harvard would present to donors a more compelling picture of itself, as an institution able to make up its own mind about its needs. This might help loosen the purse strings of corporations and of individuals who do not have a close connection with any single Harvard activity, especially if generous donors of unrestricted money were to receive appropriate recognition. Even loyal alumni of the College, or of one of the graduate schools, might respond sympathetically to a cogent presentation of the University's own well-reasoned conclusions about its priorities. Such a presentation might strengthen their sense of identification with Harvard as a whole. In any event, little would be lost since anyone firmly committed to a particular School or project could continue to earmark his gift (subject, perhaps, to some scheme of the sort suggested in the next section). At a minimum, alumni would be protected from the flood of uncoordinated solicitations from Cambridge, at best an irritant and possibly an excuse for giving little to each or nothing at all.

Here again, it is probably not a matter of either/or but of finding the right mix. The new President will wish to study the question and make up his mind quickly. Whatever he decides, he will also want to take a hard look at Harvard's machinery for fund raising. The present operation is small and places an extraordinary burden on a few dedicated people. Should not a new, well-staffed office be created, headed by a senior officer of national standing and reputation? What role should professionally trained fund-raisers play? Would it be worthwhile to ask a considerable number of alumni who are interested in the University's welfare to spend a small portion of their time working with special constituencies, and to offer them generous compensation for their efforts?

2. Is it possible to loosen the link between the way money is raised and how it is spent?

Even if we continue to rely heavily on money raised in a decentralized way, no iron law decrees that he who raises the money gets to keep all of it. The terms of each new deed are subject

to negotiation, and the center has a voice in the matter. One can think of a rich variety of devices that would give the University more power to reallocate money between Schools and joint activities, among Schools and within Schools. Harvard could stipulate that restrictions on new money carry an expiration date, the date to vary according to the narrowness of the restriction. It could "tax" the income, or capital gains, or even the original principal of gifts to low priority activities, or activities likely to become so. (For that matter, it could levy a tax on each School's income from tuition.) It could use the proceeds of such taxes to supplement, perhaps on a partially matching basis, gifts in support of high-priority projects. Such devices would of course alter the incentives of donors as well as of members of the University out to raise money for their own purposes. But the effect on incentives of any such scheme of variable taxes and subsidies would depend on its structure; the benefits of an efficiently drawn system could outweigh the costs, especially under the unit system, as long as the flow of *unrestricted* new money remains meager.*

3. What about money from the Government?

How much money will Harvard be able to raise from the Federal Government during the next decade? How much should it accept, on what terms? The answers are not clear, but some facts are:

(i) The Federal Government contributes about a third of the University's operating income.

(ii) In fiscal '69, for the first time in fifteen years, the flow of government funds to Harvard declined. In fiscal '68, government contract and grant expenditures came to $63.9 million.

* In effect, the University already taxes the tubs. It levies an annual "assessment" on at least those units of the University that earn tuition, and uses the proceeds to defray the costs of a variety of overhead activities. It would appear that the present scheme contains some quirks; the base on which the assessment is levied arbitrarily favors some activities over others. Allocation of true overhead is of course intrinsically arbitrary. But not everything that passes for overhead is a fixed cost. Variable costs should be identified and allocated.

Needless to say, the suggestions above go far beyond taxing tubs merely to cover true joint costs, and would involve a radical departure from present practice. Redistributing tuition receipts among Schools through taxes and subsidies would be an even more revolutionary change (and would raise even more difficult incentive problems).

In '69, they fell to $63.7 million, and in '70, to $61.5 million. The proportion of public money in the University's total expenditures has also declined. The downward trend may not match the upward trend of the previous fifteen years. But it would be foolish to expect a turn-around soon.

The purist solution: give up all dependence on money from Washington, is clearly not feasible in the short run (see Table II). In the long run, it is not likely to prove feasible or desirable. But the status quo is not stable. Would it not be timely for the University to establish a special task force to study the matter? What rationale is there for large-scale public support of private universities in general, and of Harvard in particular? What is the effect of such support on the shape and priorities of the University, especially in research? Are there problems of undue control that we have not yet faced? What kinds of politically defensible public support would work best?

As we have suggested earlier, the financial relation between the Federal Government and the entire higher educational system raises a host of unanswered questions. Harvard should prepare itself to play a significant role in assuring constructive answers.*

4. What "price" should students be charged for a Harvard education?

At present the University charges a "gross" price, in the form of tuition for four years, that covers only a fraction of the average cost of an undergraduate. The price charged for room and board is considerably less than the cost of capital and upkeep. The *net* price is even less; approximately half the students enrolled in the College receive scholarship aid.

Three questions arise. Should the University continue to subsidize *all* students, as it does now? If not, who should be subsidized, on what scale? And what form should the subsidy take?

* Any study of the Federal role must of course take into account such indirect means of current support as the tax-deductibility of gifts to universities. But it should also explore new forms of support, direct and indirect. A Federal role in establishing a "capital market" for student loans is one promising possibility.

Because of the financial pressures faced by the Government of the Commonwealth, we have not addressed the question of money from the State House. A proposal calling for State money is contained in *Financial Problems of Massachusetts Private Higher Education*, a report of a select committee chaired by Mr. William G. Saltonstall.

The case for some implicit subsidy for all, rich as well as poor, comes down to the effect of large increases in tuition on Harvard's ability to attract first rate students from prosperous families (and to the recognition by many such students, and their families, that they incur a moral obligation to support the University by gift). Obviously, Harvard alone cannot afford to increase its tuition by a factor of two or three. Even if competing private universities were to follow suit, there would remain the competition offered by first rate public universities. Nevertheless, this is an area worth careful study.

The more tuition we charge, the more important scholarships and fellowships become. Harvard must admit students on the basis of qualification alone, without regard to income; poor applicants must not be placed at a disadvantage. But need the subsidy to a poor student take the form of a gift rather than a low- or zero-interest loan? Insofar as a university education is a lucrative financial investment for the student, as measured by the effect on his expected lifetime income, the case for long-term loans (perhaps with repayment contingent on income) has considerable force. Insofar as the payoff is uncertain and the expected *social* gain exceeds the private – it varies field by field – there is also a case for some public subsidy.

In any event, since risks should be pooled, there is need for organization. This is an area where private universities should act together, and try to engage both their public sister institutions and the Federal Government.*

5. Can Harvard better exploit its physical plant?

Under present practice, despite summer school, most of Harvard's facilities stand idle during a significant part of the year. Are financially attractive changes possible that would not damage the quality of university life? Could the summer school be made more profitable? Again, the answers deserve careful study and periodic review by responsible senior officials of the University.

* The technical design of any such scheme calls for careful scrutiny. As always when differential pricing is combined with taxes and subsidies, one must be wary of notch-effects, arbitrary cut-offs and ceilings, and the like. The danger for a place like Harvard is that it becomes an institution populated exclusively by the rich and the very poor.

V. Money Management

In the spring of 1970, Campaign G.M. forced on the University a difficult question: does Harvard have some moral responsibility for the social conduct of corporations in which it holds stock, and if so, how can it discharge that responsibility? Student opinion favored Campaign G.M. against General Motors management. An informal poll of alumni by the *Harvard Bulletin* came out the same way.* The Arts and Sciences Faculty voted overwhelmingly, but perfunctorily, in favor of Campaign G.M. Although the Treasurer indicated strong support for G.M. management, the Corporation delayed its decision to hear argument by members of the community. In the end, the Corporation decided in favor of G.M. Recalling the entire episode, one of the Fellows is alleged to have observed that the behavior of none: students, faculty, Fellows, *appeared* responsible to the others.

The apparent irresponsibility of these groups in the eyes of one another is traceable in part to Harvard's present system for managing money – and especially to the form and content of the information that is made available to the community at large about its financial affairs. Since 1945, the University's endowment has been managed by the Treasurer, in his triple capacity as Harvard's principal financial officer, as a Fellow of the Corporation, and as the Managing Partner of the State Street Research and Management Company of Boston. The Treasurer has had not only full executive authority over the day-to-day management of the portfolio, but wide discretion over broad policy. His decisions have been reviewed bi-weekly by the other Fellows, and annually by the Overseers and also by a Committee on Administration comprised of professional financial people from the academic and business world. But the *public* reports – notably the annual report to the Overseers, which contains a detailed account of the year's transactions and of the financial state of the University – are so complicated, and so devoid of any explanation of broad policy, that anyone not regularly a party to the management of Harvard's portfolio would find it exceedingly difficult to evaluate the results. No information is given that would reveal the guidelines that inform choices: the trade-offs made between present and future, among yield and growth and risk

* The design of the poll has been the subject of some controversy.

and liquidity. Anyone interested in the underlying policies can only guess at them by inference.

It is fair to recognize that, until the recent past, the rest of the community has been content to remain ignorant. Not many members of the faculty or students have volunteered to do the hard work required to master the material. But times have changed. Both the strategy and the machinery of money management have become the subject of debate.

1. If only money mattered, what criteria would be appropriate for guiding the investment of Harvard's portfolio? And what machinery?

We have not investigated the policies that have informed the management of the portfolio; nor have we studied the record of performance. But two questions which are independent of the policies and the record of the past suggest themselves:

– First, should not the underlying guidelines be made more explicit and a matter of public record? That would enable competent members of the community to assess those guidelines, and to evaluate the translation of policy into transactions. (The new unit system of accounting will in any case make at least superficial evaluation of performance much easier.)

There would be costs as well as benefits. Exposure to carping by the unsophisticated or people with axes to grind might inhibit the manager, who has to play a long-term game where average performance is what counts, not any single move, and where the only certain gainer from frequent, large moves is the broker. But would not the benefits of engaging interested members of the faculty, and facing them with the financial facts of life, outweigh those costs?

– Second, a more specific question: is there any reason for a tax-exempt institution like Harvard to distinguish between dividends and interest, on the one hand, and realizable capital gains on the other? The distinction makes no economic sense. After the fact, and at any point in time, a dollar of realizable capital gains (net) is exactly equivalent to a dollar of "income." It has been argued that the distinction is imposed not by economics but by law. Some who should know believe that, if the issue were brought to a head, the courts would rule the other way on most of the portfolio. Others, at least as

knowledgeable, strongly disagree. The operative question is whether the issue should be tested.

To recognize that the distinction makes no economic sense is not to argue that Harvard should regularly spend legally spendable capital gains, or even all of its interest and dividends. The question of how much should be spent and how much saved for the future should be faced as such, a matter of high policy. There is a strong *prima facie* case for reinvesting at least enough of the total return to ensure that the corpus of the endowment is protected in real terms in the face of the 5–8% cost inflation to which the University has been subject. There exist a number of devices (buffer reserves, moving averages, and the like) to take account of the fact that the securities market is a two-way street. Such devices could be used to protect the endowment from erosion, and the University from a roller-coaster cycle of stop-and-go, of feast and famine.

On machinery. No matter how well the present arrangement has done by Harvard, it would seem appropriate for the Governing Boards to commission a careful study, by an external committee, of whether any changes should be made. We have already suggested one of the central questions: should the task of portfolio management be more sharply separated from the task of setting broad policy and reviewing performance? What would be the cost of any such change, given that State Street Research has provided its services for a very small fee? (Some have argued that Harvard should have an investment committee other than the Corporation itself. And some believe that the endowment should be split among two or three managers who would then compete. In our judgment, the latter is probably not a good idea. It would be difficult to design incentives for competing managers that would not bias them in favor of spectacular performance at high risk.)

A second question – which violates the premise that literally only money matters – concerns *profitable* social investment. Should Harvard set up special machinery to seek out investment opportunities that are financially competitive but yield extra social benefit as well? The issue raises two specific questions of fact: (1) how abundant are such opportunities? (2) are they profitable enough to cover the extra cost of the elaborate entre-

preneurial effort required to find them and make them turn out right? (Recent corporate experience in this area suggests caution, especially since, in contrast with say IBM, any losses the University may suffer would not be shared 50–50 by the U.S. Treasury.)

2. If not only money matters, what financial guidelines should Harvard observe? What machinery would be appropriate for selecting those guidelines and supervising their application?

President Pusey has appointed a committee chaired by Professor Austin to make recommendations on this subject. We will not attempt to anticipate the Austin Committee's conclusions; suffice it to suggest some of the difficulties.

What ethically defensible guidelines would permit one to score the relative "virtuousness" of the social conduct of a corporation in which Harvard owns stock? Can the University learn enough about the net social impact of the hundred odd companies in which it invests to make judgments that will neither be, nor seem to be, capricious? If it explicitly brands some companies ineligible on social grounds, does not the University implicitly confer virtue on others whose stock it continues to hold? Can one devise some readily applicable rules of thumb that permit quiet sorting of hundreds of companies? Sophisticated criteria are likely to require elaborate machinery for gathering and processing information. Relatively simple, low cost machinery could cause the University to make decisions that are both intellectually and ethically shabby.

Can one defend an opportunistic strategy: judging corporate conduct only when the question is forced on the University from the outside? Where Harvard's action is not likely to have real effect, should it make symbolic gestures for their own sake? Alternatively, can the University try to make a real difference, even when the size of its investment does not give it much leverage, by taking the lead in rallying other stockholders? What would be the consequences for the raising of new money, and, if quasi-political questions are involved, for Harvard's tax exemption?

Some of the questions bear on Harvard's decisions about what stocks to buy, hold, and sell. Some apply to the more difficult and, in a sense, inescapable choice the University faces

when voting its stock on controversial issues. The difficulties seem great. Yet the Treasurer and the Corporation make judgments of this sort, at least implicitly, both as a part of their over-all evaluation of a company's management and prospects, and in their decisions about how to vote at stockholders' meetings. But – and this is the critical point – as a general rule the decisions are not a matter of any announced University policy. How such judgments could be made both more explicit and publicly defensible, with wider participation by the community, is unclear. At least in the case of front-page proxy fights, however, there is no obvious strategy that avoids the dilemma. The problem, once again, is to explore whether there exists machinery that will assure well-reasoned, equitable and widely acceptable choices.

We await the Austin report.*

* Some have suggested that private universities, foundations, and others who face this problem, join forces in providing themselves with careful, hardheaded staff work that would enable them to vote their stock on the basis of a patently responsible examination of the merits of the case. That would certainly permit better informed votes. And it would recognize that, when it comes to voting as against holding stock, only symbolic neutrality is possible; in most cases, abstention is the equivalent of a vote for the management. On the other hand, would it not be politically dangerous for large, private, tax-exempt organizations to assume the role of policing the social conduct of other private institutions? Many people feel that that job belongs to the government.

One might explore an alternative strategy that minimizes any guilt by association and also any leverage Harvard might have on companies in which it does invest. It would require Harvard to keep its share in any particular company at such a low level that the University's influence would be unmistakably negligible. In fact, most of Harvard's investments already meet that test. However, such a strategy would also require that no officer of the University be involved in making judgments about the purchase and sale of particular securities, and that neither officers of the University, nor its investment managers, sit on the board of any corporation by virtue of Harvard's holdings.